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No. 74-1427

In the Supreme Court of the United States

OCTOBER TERM, 1975

REUBEN L. ANDERSON-CHERNE, INC., APPELLANT

v.

THE COMMISSIONER OF REVENUE OF THE STATE OF MINNESOTA

ON APPEAL FROM THE SUPREME COURT OF MINNESOTA

MEMORANDUM FOR THE UNITED STATES AS AMICUS CURIAE

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This memorandum is submitted in response to the Court's invitation of June 23, 1975, requesting the views of the United States.

Appellant is a Minnesota corporation, with its principal office in Minneapolis, Minnesota, and is engaged in business in that State. It is, and has been, subject to the "annual excise tax * * * imposed [by Minn. Stat. Ann., Section 290.02 (1962) (J.S. 3)] upon every domestic corporation * * * for the privilege of existing as a corporation during any part of its taxable year." As that statute provides, "[t]he tax so imposed shall be measured by such corporations' taxable net income for the taxable year for which the tax is imposed" (J.S. A8-A9).

Appellant filed corporate excise tax returns with the Commissioner of Taxation of Minnesota for its fiscal years ending March 31, 1968, 1969, and 1970, and paid the amounts shown to be due. In those returns, it included in its taxable income for the respective fiscal years $22,310, $45,874, and $93,880, of interest income it had received from United States Treasury notes and other obligations of the United States. In including such interest in its taxable income for purposes of the Minnesota tax, appellant complied with applicable statutory requirements. Although Minn. Stat. Ann., Section 290.08, subdivisions 7 and 8, excludes interest upon obligations of the State of Minnesota and its political subdivisions and of the United States and its instrumentalities, it does so only for purposes of the tax on corporations not subject to the excise tax at issue here. Thus, subdivision 13 of Section 290.08 explicitly provides that the exclusion shall not apply to corporations taxable under Section 290.02 (J.S. A8-A9; J.S. 3-4).

Appellant petitioned the Commissioner of Taxation for refunds for its fiscal years 1968, 1969, and 1970, of $2,512.85, $3,134.53, and $2,391.96, respectively, on the ground that interest from obligations of the United States is immune from state taxation under Section 3701 of the Revised Statutes of the United States, 31 U.S.C. 742. The Commissioner denied a refund (J.S. A2-A3). The Tax Court of the State of Minnesota (J.S. A1-A6) and the Supreme Court of Minnesota (J.S. A7-A14) upheld the Commissioner of Taxation on the ground that Minn. Stat. Ann., Section 290.02, imposed a nondiscriminatory franchise tax, and that Section 3701 of the Revised Statutes excepts a nondiscriminatory franchise tax from the prohibition it otherwise imposes.

1. Section 3701 of the Revised Statutes, as amended, 31 U.S.C. 742, provides as follows:

> All stocks, bonds, Treasury notes, and other obligations of the United States, shall be exempt from taxation by or under State or municipal or local authority. This exemption extends to every form of taxation that would require that either the obligations or the interest thereon, or both, be considered, directly or indirectly, in the computation of the tax, except nondiscriminatory franchise or other non-property taxes in lieu thereof imposed on corporations and except estate taxes or inheritance taxes.

The first sentence of the statute originated in Section 2 of the Act of February 25, 1862, 12 Stat. 345-346. The second sentence was added by Section 105(a) of the Act of September 22, 1959, 73 Stat. 622.

Even before this statutory enactment, this Court had held in *Weston* v. *City Council of Charleston*, 2 Pet. 449, that obligations of the United States could not, under the Constitution, be subjected to a state or local property tax. See *Society for Savings* v. *Bowers*, 349 U.S. 143, 144.

However, the Court has also held, in an extended series of decisions, that neither the Constitution alone nor Section 3701 as it existed prior to 1959 prohibits a state from measuring a corporate franchise or privilege tax by property or net income that includes obligations of the United States or the interest therefrom. In *Werner Co.* v. *Director of Taxation*, 350 U.S. 492, the Court summarized this series of decisions as follows (350 U.S. at 494):

> And since this is a tax on the corporate franchise, it is valid despite the inclusion of federal bonds in the determination of net worth. This Court has consistently upheld franchise taxes measured by a yardstick which includes tax-exempt income or property, even though a part of the economic impact of the tax may be said to bear indirectly upon such income or property. See, *e.g.*, *Society for Savings* v. *Coite*, 6 Wall. 594; *Provident Institution* v. *Massachusetts*, 6 Wall. 611; *Hamilton* v. *Massachusetts*, 6 Wall. 632; *Home Ins. Co.* v. *New York*, *supra*; *Educational Films Corp.* v. *Ward*, *supra*; *Pacific Co.* v. *Johnson*, *supra*.

Similarly, the Court in *Flint* v. *Stone Tracy Co.*, 220 U.S. 107, upheld the federal tax upon doing business in corporate form imposed by Section 38 of the Act of August 5, 1909, 36 Stat. 11, 112, even though it was measured by net income including interest from state obligations.

The 1959 amendment of Section 3701 of the Revised Statutes (31 U.S.C. 742) made no change relevant to this case. In effect, it codified the decisions of this Court when it explicitly excepted nondiscriminatory franchise taxes imposed on corporations. As the legislative history makes clear, the amendment was adopted to counter the position of one state with respect to the inclusion of interest on obligations of the United States in the computation of its net income tax.[1]

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[1]The pertinent committee reports state as follows:

> Present law provides that obligations of the United States are to be exempt from taxation by or under State or local authority. The Supreme Court has held that this includes the exemption of interest on U.S. obligations from taxation by or under State or local authority. It has been pointed out to your committee, however, that one State has taken the position that the statute as now worded does not prohibit a State from including interest on Federal obligations in computing "gross income" upon which taxable net income is determined. The bill (sec. 105) makes it clear that the exemption for Federal obligations extends to every form of taxation that would require either the obligation, or the interest on it, or both to be considered directly or indirectly in the computation of the tax, except nondiscriminatory franchise taxes (or other nondiscriminatory non-property taxes imposed in lieu thereof) on corporations and except estate or inheritances taxes. [H.R. Rep. 1148, 86th Cong., 1st Sess., p. 8 1959); S. Rep. No. 909, 86th Cong., 1st Sess., p.8 (1959).]

2. It is therefore clear that if the tax imposed by Minn. Stat. Ann., Section 290.02, is a nondiscriminatory franchise tax, as the courts below held, there is no constitutional or statutory basis for challenging the inclusion of interest from obligations of the United States in the net income that is the measure of the tax.

Appellant appears to have contended, however, that the tax here is not a franchise tax, but a property tax or an income tax (J.S. A4-A6, A10-A14, A15). There is, however, little support for that position. The statute imposes an "annual excise tax." The Supreme Court of Minnesota held that the tax is a franchise tax (J.S. A12-A14). While those categorizations are not necessarily controlling here, there is no reason for rejecting the Minnesota Supreme Court's construction of the statute as imposing a franchise tax. See *Werner Co.* v. *Director of Taxation*, *supra*, 350 U.S. at 493; *Gurley* v. *Rhoden*, No. 73-1734, decided May 12, 1975, slip op. 7-8; cf. *United States* v. *Mississippi State Tax Commission*, No. 74-548, decided June 2, 1975, slip op. 8, 9, n. 7.

The operative terms of the statute define its incidence, and demonstrate the character of the tax. They provide that, with respect to domestic corporations, the tax is upon the privilege of existing as a corporation, and, with respect to foreign corporations, the tax upon the priv-

ilege of doing, or the doing of, local business in corporate form. Such a tax is the very archetype of a franchise tax. See, *e.g. Pacific Co.* v. *Johnson*, 285 U.S. 480, 489-491; *Educational Films Corp.* v. *Ward*, 282 U.S. 379, 385-392; *Flint* v. *Stone Tracy Co.*, *supra*, 220 U.S. at 161-165. See also *Colonial Pipeline Co.* v. *Traigle*, No. 73-1595, decided April 28, 1975.[2]

3. In its notice of appeal (J.S. A15), appellant also claims that the tax discriminates against those corporations subject to this excise tax, as opposed to those corporations subject to the net income tax of Minn. Stat. Ann., Section 290.03. This point was, however, not raised below (J.S. A10). But at all events, appellant's suggestion of discrimination is not relevant to Section 3701 of the Revised Statutes.

The Minnesota statute only makes the distinction required by the constitutional decisions of this Court (see, *e.g., Northwestern Cement Co.* v. *Minnesota*, 358 U.S. 450) between corporations subject to the franchise tax and those corporations subject to a net income rather than a franchise tax because their business consists exclusively of foreign or interstate commerce. Compare Minn. Stat. Ann., Section 290.02, with Section 290.03.

For the reasons stated, this appeal presents no substantial federal question. It is therefore respectfully submitted that the appellee's motion to dismiss the appeal should be granted.

ROBERT H. BORK,
Solicitor General.

AUGUST 1975.

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[2]Beginning January 1, 1975, Section 290.02 was amended to impose [a]n annual income tax * * * for the privilege of existing as a corporation during any part of its taxable year, and upon every foreign corporation doing business within this state * * * ." Despite the change of terminology from "excise" to "income," the operative terms of the statute are still upon the privilege of exercising the corporate franchise. Thus, the tax is still an excise tax under the criteria of this Court's decisions.